Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
Connect America Fund	)	WC Docket No. 10-90
	)	
ETC Annual Reports and Certifications	)	WC Docket No. 14-58
	)	
Developing a Unified Intercarrier Compensation Regime	)	CC Docket No. 01-92

COMMENTS OF THE KANSAS CORPORATION COMMISSION SUPPORTING THE FCC'S INITIATIVES REGARDING EXPENSES, COST ALLOCATIONS AND AFFILIATE TRANSACTIONS

1. The Kansas Corporation Commission (KCC) is the governmental agency in Kansas charged with regulating telecommunications carriers' intrastate rates and disbursing state-level universal service support for carriers in high-cost areas.

2. Having dealt with a multitude of issues touched upon by the Federal Communications Commission's (FCC's) March 30, 2016, *Report and Order, Order and Order on Reconsideration, and Further Notice of Proposed Rulemaking* (Order), the KCC welcomes the opportunity to submit comments.

3. As recognized by the FCC in Paragraph 328 of its Order, the telecommunications landscape has become increasingly complex since 1996. Regulated carriers no longer offer just plain-old telephone service (POTS). Regulated carriers also offer an array of services including POTS, Internet, Cable TV, VoIP, Wireless service, and long-distance. Oftentimes, unregulated services are provided through an affiliate pursuant to agreements with the regulated entity. This new landscape certainly "impact[s] the types of costs carriers attempt to include in their revenue requirement and the ways in which carriers allocate costs between regulated and non-regulated services and affiliates." The KCC's experience has indicated that the current rules and

regulations allow, and actually incentivize, carriers to include unregulated costs in regulated accounts to increase their revenue requirement and universal service subsidy. Thus, the KCC supports the FCC's efforts to address the issues raised in its Order.

4. With that in mind, the KCC will be commenting upon the discussions had in Paragraphs 327 through 363 of the Order.

A. Permitted Expenses

5. The KCC supports the FCC's initiative of reviewing and excluding investments and expenses that are not necessary for the provision of regulated telecommunications services. The KCC also agrees that the terms "used and useful," "prudent expenditure," and "necessary to the provision of" should be clarified to ensure a consistent standard for determining properly-included investments and expenses, and promote "a business operation that is run efficiently to provide telecommunications services."

6. The expenses identified in Paragraphs 340 and 342 of the Order are not necessary for the efficient provision of regulated telecommunications services and should not be included in the determination of revenue requirements, nor should these expenses be subsidized by the general public through universal service support mechanisms.

7. In addition to the types of expenses identified by the FCC, the KCC's experience has shown the attempted inclusion of expenses such as season tickets to sporting events, sponsorships for charity events, utility bill payments for employees, and corporate image advertising. Furthermore, some companies include expenses for trips during the year to attend national, regional and local industry-related organizational meetings and/or training events. The KCC understands the importance of staying abreast of current events and having a trained workforce; however, it may not be reasonable for a carrier's regulated revenue requirement and

publicly funded universal service support to bear all of the travel expense related to these events, especially if such expenses benefit non-regulated operations. Thus, the KCC suggests the FCC consider additional rules (e.g. a cap on regulated/subsidized "business" travel, allocation between operations and/or to shareholders, etc) to address the amount any regulated entity may include in its revenue requirement.

8. As far as how to implement exclusion of these expenses from both revenue requirements and universal service support, the KCC submits that a regulation detailing which expenses may not be included is appropriate. However, the FCC should clarify that any itemized list of excluded expense may not be all inclusive and that it is the carrier's responsibility to ensure that only those expenses necessary to the provision of regulated services may be included in its revenue requirement and universal service support filings.

B. Executive Compensation/ General Employee Payroll

9. With respect to Paragraph 345 of the Order, the KCC submits that a sufficient level of executive compensation should be included in a rate-of-return carrier's revenue requirement for purposes of determining rates and high-cost support; however, the amount should reflect the efficient operations of a regulated business. Any excessive levels of such compensation, including wages and benefits, should be reined in.

10. The amount of executive compensation and, in fact, the compensation paid to any employee, is a management decision. However, the level of such compensation included in the regulated revenue requirement should not burden universal service mechanisms to the benefit of a few. To address this issue, the KCC has more recently relied on a comparison of an executive or employee's pay to a national average based on data reported by carriers for similar positions at similarly-sized companies. Other methodologies, including a cap on compensation or

productivity metric, could be used to determine a sufficient level of executive/employee compensation.

11. The FCC could consider a minimum and maximum number of executives/employees and/or the compensation recognized in the revenue requirement based on the number of customers served and/or revenue earned by the regulated entity, the geographic location and cost of living, etc. For example, assume two regulated entities serve an identical number of customers and are similarly situated geographically. Company A has 5 executives and 15 employees, $2 million in regulated revenue and annual payroll of $1.5 million. Company B has 3 executives and 12 employees, $4 million of annual regulated revenue, and total payroll of $1.0 million. Company A and B's revenue requirement and universal service support subsidy are based purely on each company's management decisions regarding employment numbers and compensation. This approach does not take into consideration the reasonableness of the compensation reported, the number of employees needed to efficiently run a regulated business, or the level of revenues earned by the carrier.

12. If the FCC adopts a mechanism to limit the number of executive/employees' compensation or an overall compensation dollar amount to be included in the revenue requirement, the company would receive a certain dollar amount and its management could then decide how best to use the money to support its regulated operations, just as management makes the employment and compensation decisions. Whatever methodology is adopted, however, should not continue to rely on, or promote, the current process whereby an increase in compensation automatically results in an increase in the revenue requirement and resulting universal service support recovery.

13. Finally, with respect to payroll, companies have incentive to attempt to collect universal service support for employee positions that are not necessary to providing sufficient and efficient regulated telecommunications service. For example, a company may hire family members and create new positions (e.g. community ambassadors, seat on the board, another management position, etc.), thus, the FCC should keep a keen eye out for these types of positions and ensure that only those necessary for efficient operations are allowed in revenue requirements and universal service support determinations.

C. Board of Directors

14. With respect to Board of Directors' expenses, the KCC submits that the FCC should carefully evaluate the relationship between board members and employees. A carrier serving in a very rural, sparsely populated area or a family-owned company may have a CEO that is also sits on the board of directors, thereby, determining his or her own salary.

D. Plant Held for Future Use

15. With respect to Paragraphs 348 and 349, the KCC supports a change in the rules that reduces the two (2) year utilization requirement down to one (1) year. It is possible for a carrier to begin a project and due to circumstances beyond its control (e.g. developer of a new housing complex files bankruptcy), fail to complete the project. If a project is not completed and the plant will not be "used and useful" by the carrier's customers within one (1) year, customers and the public generally should not have to cover the costs through rates or subsidies.

E. Consultant Identification

16. The KCC supports a rule that requires rate-of-return carriers to identify their cost consultants in their Form 481s. A consultant often prepares reports for more than one client,

thus, if the consultant errs on one carrier's filing, a similar error may flow through and affect multiple carrier's filings. Each affected carrier's filings would need corrected.

F. Cost Allocations

17. With respect to Paragraphs 353 through 355, the KCC agrees that cost allocation needs to be examined. Specifically, as the FCC points out, "there is an incentive to interpret the allocation rules in order to allocate as many costs as possible to their regulated activities, both to justify a higher interstate revenue requirement and to receive additional high-cost support."

18. As recognized by the FCC, changes in the telecommunications industry have resulted in traditional rate-of-return regulated carriers now offering both regulated and non-regulated services or sharing facilities, employees, and expenses between affiliates, with appropriate cost allocations playing a critical part in the determination of the revenue requirement and universal service support. For example, a regulated carrier may have employees that work for both the regulated telephone company and the non-regulated company that provides Internet, cable television, and wireless phone service. In spite of the FCC's rules for allocating costs and time reporting (e.g. allocations, direct or positive time reporting, etc.),[1] KCC audits have found instances where employees, including executives, have not recorded their time between the regulated and non-regulated operations. Other instances have occurred where an executive who manages both regulated and non-regulated businesses claimed that upwards of 75% of the time worked was for the regulated service. Given the nature of consumer-driven cable and Internet services, it may appear unreasonable for the executive to spend 25% or less of his work time on un-regulated activities. Thus, in spite of the FCC's time reporting rules, the current system does not encourage strict adherence to such rules.

[1] 47 C.F.R. § 64.903.

19. The FCC could consider placing a cap on or determining a maximum threshold level for a percentage allocation of an executive's time to regulated services. For example, the FCC could set a threshold allocation based upon relative revenues. If a company derives $1,000,000 in revenues from non-regulated services and $100,000 from regulated telephony, the company would be allowed to allocate at most 10% of an executive's time to supported expenses.

20. Carriers often use the same plant, property, and equipment to jointly offer regulated and non-regulated services. The FCC has allowed carriers to choose from several methodologies, based on their company-specific situation. However, this approach allows a significant amount of leeway in determining what a "reasonable" allocation is. For example, in Kansas, cost allocations have been based upon loop capacity, time studies, and/or the number of regulated to non-regulated company and affiliate lines.

E. Affiliate Transactions

21. With respect to Paragraph 358 of the Order, the KCC submits that carriers should be explicitly required in the FCC's regulations to have written contracts between its affiliates so that costs may actually be audited and compared to fair market prices. The KCC has seen countless instances where carriers do not properly comply with Part 64 rules regarding the determination of fair market value or fully distributed cost. Furthermore, if the FCC determines specific costs of the regulated entity should not be recovered via its revenue requirement, those same costs should be excluded when determining joint and common costs, including costs associated with affiliated transactions; to do otherwise would allow indirect recovery of such costs.

F. Non-Affiliate Transactions

22. With respect to non-affiliate transactions, the KCC agrees it is prudent to consider whether non-affiliate transactions should be scrutinized, especially when the owner of the non-affiliated company is related to an owner, employee, or Board of Director member of the telecommunications carrier. Where such circumstances arise, rules similar to those governing affiliate transactions may be appropriate.

G. Compliance Issues

23. The FCC should require both the person filling out the applicable forms and an officer of the Company to annually certify, under penalty of perjury, that all FCC regulations, including those governing prohibited expenses, affiliate transactions, and cost allocations, have been complied with. If it is determined that a filing does not comply with the FCC's rules and regulations, enforcement action should include corrective filings and refunds as applicable upon the first instance for non-willful violations. For willful violations, consideration should include repayment of any universal service support subsidies.

H. Enforcement

24. To address violations of the rules, enforcement actions are necessary. The FCC should strengthen its enforcement actions with regards to violations of its rules. Public funds should be safeguarded and only provided when necessary to achieve the goals of advancing universal service. When carriers violate the FCC's rules, the underlying basis for the violation, rather than the amount of discrepancy, should be of first concern. If there is a willful violation, the company should be subject to fines and penalties, and a probationary period in which it is subject to audit. Ultimately, if a second willful violation occurs, the FCC should consider disbarment from participating in NECA pools or receiving universal service funds altogether.

I. Conclusion

25. The KCC appreciates the opportunity to comment on these matters of national importance. The KCC agrees that all areas discussed by the FCC in its Order need to be re-evaluated in light of the changed telecommunications landscape.

Respectfully submitted,

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Jay Scott Emler, Chairman of the Kansas Corporation Commission (abstaining)

Shari Feist Albrecht
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Shari Feist Albrecht, Commissioner

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Pat Apple, Commissioner